

DPD-3714-59

4 June 1959

MEMORANDUM FOR THE RECORD

SUBJECT : Final Settlement Negotiations of Contract No. HF-1230
with The Firewel Company, Inc.

1. On 27 May 1959 Messrs. [redacted] and [redacted] the AF Site Auditor and [redacted] USAF, in Buffalo, New York to discuss the final cost audit report and to plan final settlement negotiations of Contract No. HF-1230 with The Firewel Company Inc., Buffalo, N. Y.

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2. The Contractor's final cost proposal for performance of the redeterminable portion of Contract No. HF-1230, i.e. Schedules 1 and 2, is \$639,476. The contract target price and ceiling price for Schedules 1 and 2 combined is \$587,309 and \$646,040, respectively. The AF Auditor in his final report questioned \$89,007. See Advisory Report on Price Redetermination Audit, #475, dated 21 May 1959.

3. On 28 May 1959 the scheduled meeting was held at The Firewel Company, Inc. Buffalo, New York to negotiate final settlement of the contract. In attendance were Messrs, [redacted]

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program.

4. [redacted] opened the meeting stating that the claim of the subcontractor, David Clark Co., for performance of Schedule 1 of the contract in the amount of \$248,113 had been approved and that the Contractor should negotiate settlement with the subcontractor. Mr. [redacted] then pointed out to the Contractor's representatives the main areas under which cost had been questioned by the Auditor under the prime contract, such as:

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a. Direct Labor which could not be audited for 1956 and 1957 as the Contractor did not have adequate records for these years and had used estimated amounts.

b. Manufacturing Burden which the Contractor had applied to purported direct labor on an unsupportable direct labor hour basis. Further, that costs included in the Manufacturing Burden such as bonuses, general research, capital expenditures, entertainment and insurance could not be charged to Government contracts. (see Exhibit B of Report #475)

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25 YEAR RE-REVIEW

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c. Engineering Overhead which had been established by the Auditor by reclassification of engineering overhead accounts from the general and administrative expense pool. In this way a more realistic cost distribution was effected. In this account, labor and other expenses pertaining to general research and development were disallowed as not necessary in the performance of Government contracts. (See Exhibit C of Report #475)

d. Allocation of General and Administrative expense on the basis of sales. This method of allocation was objectionable and therefore General and Administrative expense was combined into one pool and allocated on the basis of cost of sales. Items of General and Administrative expense claimed by the Contractor such as selling expense pertaining to Contractor's furnace division, bonus payments to officers, entertainment included in travel expense, donations, expenses listed under Legal and Professional Expenses, advertising, and life insurance were not recognized as necessary for performance of Government contracts.

e. Other Costs and Profit - It was pointed out to the Contractor that with respect to its subcontractor's costs pertaining to the David Clark Co., for performance of Schedule 1 of the contract a General and Administrative expense and a profit allowance of 6% and 3% respectively, were allowable in accordance with its agreement of 3 February 1956 in lieu of normal G&A expense and 10% profit as included in the Contractor's cost proposal.

5. In response to the foregoing [] pointed-out that upon inception of the contract and for approximately two years thereafter his organization had inadequate records to record cost under the contract. [] acknowledged the fact that he had received a letter from the Contracting Officer dated 11 April 1956 inclosing Part 2 of Section XV, Contract Cost Principles, from the ASPR, for use as a guide in recording costs under Contract No. HF-1230, and that as a result of this letter and requests from Project personnel he employed an accountant in mid 1956 at which time an accounting system, which he assumed would be adequate, was initiated. Mr. [] further pointed out that Project personnel were aware of the fact that his organization did not have an approved accounting system at the time the contract was awarded, however, this was considered by all concerned as secondary in view of the urgency for development and production of the contract work.

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6. The initial offer made to The Firewel Company was \$508,734 and was based on excluding for the Contractor's claim \$89,007 representing costs questioned by the Auditor and \$32,836 representing adjustments in G&A Expense and Profit to the 6% and 3% applicable to the David Clark Company's subcontract.

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7. [] declined this offer and pointed out that with respect to labor costs the learning curve on many items was as much as 200% and that maximum efforts were exerted by him and his engineers to meet Project requirements. [] stated that in view of his lack of proper accounting procedures during 1956 and 1957 that his recoveries through overhead were insufficient to cover costs properly allocable to overhead. The Contractor concurred in its prior agreement as to the 6% and 3% handling charge on the David Clark Company's sub-contract and stated that the application of normal G&A and 10% profit was included in his proposal through error.

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8. The Contractor then proposed that settlement be made in the area between its claim of \$639,476 and Contracting Officer's offer of \$508,700, or at \$574,000.

9. The Contractor's proposal was not acceptable; however, consideration was given to the merits of its labor claim and supporting arguments. Based on allowing the questioned labor cost and applying approved G&A expense and a 10% profit factor thereto, an amount of \$32,600 (approximately) was added to the Contracting Officer's initial proposal resulting in a revised offer of \$540,000.

10. The Contractor refused this offer and upon request from the Contracting Officer to state the amount it would accept as fair and reasonable settlement of the contract, proposed the amount of \$560,000. The contractor requested that this amount be considered in collaboration with the negotiators and technical personnel who were aware of the contract and of performance thereunder from its inception. It was agreed that negotiations would be concluded at this point and that further consideration would be given the Contractor's proposal of \$560,000 as requested. The meeting was then adjourned.

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of labor employed on the contract and as to the maximum efforts extended by the Contractor in the early phases of the contract. [] stated that without the outstanding cooperation and efforts of the Contractor in developing and producing the contract items the Project would never have been operational within the schedules demanded by the Government.

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12. On 2 June 1959 the Contractor's proposal was discussed with Mr. [] who handled the initial negotiations with The Firewel Co. and was aware of the Contractor's outstanding technical performance of the work during the critical stages of the Project. [] also concurred in the Contractor's contentions as to exerting maximum efforts in the technical performances of Contract No. HF-1230.

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13. In view of the foregoing, it was concluded by the Contracting Officer that the Contractor's accounting records did not reflect the complete and overall cost of performing the contract, therefore since

the Contractor's revised proposal is \$27,309 below the contract target price of \$587,309, and since the Contractor's outstanding technical performance of the contract work must be recognized, final settlement of Schedules 1 and 2 of Contract No. HF-1230 for the total sum of \$560,00 was considered by the Contracting Officer to be fair and reasonable.

[Redacted]

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CONCUR:

[Redacted]

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Contracting Officer

DPD-DD/E [Redacted]

Distr.

1-HF-1230 T&P

1-Finance

1-Chrono

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